

ST 99-9

Tax Type: ROT

Issue: Machinery & Equipment Exemption (Photoprocessing)

**STATE OF ILLINOIS
DEPARTMENT OF REVENUE
OFFICE OF ADMINISTRATIVE HEARINGS
SPRINGFIELD, ILLINOIS**

**THE DEPARTMENT OF REVENUE
OF THE STATE OF ILLINOIS**

v.

TAXPAYER, INC.

Taxpayer

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Docket No. 96-ST-

IBT #

NTL #

NTL #

Claim for Credit or Refund

FINAL ADMINISTRATIVE DECISION

Appearances: Charles Hickman, Special Assistant Attorney General, for the Department of Revenue of the State of Illinois; Amy M. Faber and Lewis Striebeck of the Stolar Partnership for TAXPAYER Inc.

Synopsis:

This case concerns whether equipment that processes and produces digital images qualifies for the photoprocessing exemption under the Use Tax Act (35 ILCS 105/1 et seq.). The Department of Revenue ("Department") conducted an audit of TAXPAYER, Inc. ("taxpayer") for the time periods of July 1, 1991 to November 30, 1993 and December 1, 1993 to December 31, 1994 and concluded that the taxpayer owed additional tax on various items. The Department issued two Notices of Tax Liability (NTLs), which the taxpayer timely protested. The taxpayer subsequently paid the tax and filed a Claim for Credit or Refund, which was denied by the Department. The taxpayer's protest of the Department's Notice of Tentative Denial of Claim was consolidated with

the present case. An evidentiary hearing was held during which the taxpayer contended that use tax is not owed on certain specified equipment because the items qualify for the photoprocessing exemption or, in the alternative, the manufacturing machinery and equipment exemption. As a result of the hearing held, a recommendation for disposition was submitted to me, as Director, for consideration.

ISSUE:

The issue in controversy here is whether “digital photography” is “photoprocessing” as that term is defined in Section 3-15 of the Use Tax Act (35 ILCS 105/3-15). Related to this issue is whether the equipment used in digital photography is “photoprocessing machinery and equipment” as that term is defined in Section 3-5 of the Use Tax Act (35 ILCS 105/3-5).

Upon due consideration, the recommendation of the administrative law judge (“ALJ”) “digital photography” is photoprocessing cannot be accepted. As a result, I cannot accept the ALJ’s conclusion that certain equipment used in digital photography qualifies for the statutory exemption afforded photoprocessing machinery and equipment.

In reaching a conclusion that rejects the ALJ’s ultimate conclusion as to the nature of digital photography, I remain mindful of my responsibilities to the taxpayer as well as to the State. My decision is based solely upon those legal conclusions that may be fairly drawn from the competent evidence produced at hearing.

I have reviewed with particularity all evidence offered. Additionally, I have apprised myself of those pertinent provisions of State law and regulations related to the exemption sought and have considered the entire transcript of record, including, but not limited to, the testimony of witnesses and argument of counsel.

With due regard to the recommendation of the administrative law judge, I have determined that a sufficient record of proceedings was made to permit the appropriate review and issuance of a final administrative decision which differs from the initial recommendation, in accord with the provisions of 86 Ill. Adm. Code, Ch. I, Section 200.130. See also *Highland Park Convalescent Home v. Health Facilities Planning Commission*, 217 Ill. App. 3d 1088 (2nd District. 1991)

FINDINGS OF FACT

1. The taxpayer's equipment is used at various portrait studios, such as SMILE PRETTY STUDIOS in FICTITIOUS CITY, Illinois. (Tr. pp. 39-40, 71-72)

2. When customers arrive at the portrait studios to have their picture taken, they are escorted into a sitting room. The equipment that is at issue is located in this room, except for the Pentium computer and the Sony printer. The operations that take place in this room are known as "Stage 1" of the process. (Taxpayer Ex. #2; Tr. pp. 14, 57)

3. Once a customer is in the sitting room, the photographer sets up an information file (a/k/a a computer file or film file) for the customer. The photographer creates this file by typing certain information (e.g., the customer's name, the photographer's code, the studio number and sitting number) into the NCR computer. (Tr. pp. 21-22, 56-57)

4. When the customer poses for a picture, the photographer presses a "trip button," which is located on a hand-held device called the control handle. Once the trip button is pressed, this triggers two separate but simultaneous methods for taking the customer's picture. One method is referred to by the taxpayer as the "traditional" method; the other is the "freeze frame" method. Even though the two methods are

separate, they are set up so that they simultaneously take the same picture of the customer. (Tr. pp. 49-53)

5. Under the traditional method, a 35 millimeter camera is used to take a picture of the customer. When the photographer presses the trip button, this sends a signal to the “base power supply” (a/k/a the freeze frame power supply), which then sends a signal two ways at the same time: one signal tells the 35 millimeter camera to open the shutter to expose the film, the other signal goes to the freeze frame equipment. (Tr. pp. 13, 49-53)

6. Under the traditional method, the 35 millimeter camera captures an image onto its film. When the silver salts emulsion film is exposed, it captures light data chemically. The exposed film from the camera is subsequently sent to a plant in St. Louis, Missouri for processing. (Tr. pp. 42-44, 59)

7. Under the freeze frame method, equipment is used to process digital images, and a heat offset printer produces pictures of the digital images within minutes after the photographer presses the trip button. (Tr. pp. 13, 75-76)

8. Under the freeze frame method, the pressing of the trip button sends a signal to the base power supply, which sends a signal to the Zyco controller. The Zyco controller tells the Kodak 4000 CCD video camera (“video camera”) to acquire an image. This happens at the exact same time that the base power supply tells the 35 millimeter camera to open the shutter. (Tr. pp. 49-53)

9. The base power supply provides power to various items of the whole system. It was designed to interface with the freeze frame equipment. The base power supply receives current from a source such as a wall outlet and converts some of it to direct

current; it redistributes the power, sometimes at lower voltages for some of the equipment. (Taxpayer Ex. #6; Tr. pp. 17-18, 45-48)

10. The base power supply also generates a signal to the equipment to discharge the strobe or the flash tubes when the shutter of the 35 millimeter camera opens. (Tr. pp. 47-48)

11. The base power supply provides power to the control handle and the 35 millimeter camera. It also powers a black and white video camera and the motors that are used to position the camera system. The black and white video camera is used to ensure that the customer is in the proper position. None of these items are at issue in this case. (Tr. pp. 17-18, 45-48)

12. Prior to the installation of the freeze frame equipment, there was a power supply that received a signal from the control handle and sent a signal to the 35 millimeter camera to trip the shutter. It also powered the motors and the black and white video camera. This power supply did not interface with freeze frame equipment. (Taxpayer Ex. #6; Tr. pp. 17-18, 45-48, 51)

13. The base power supply does not power the Zyco controller, the Zyco ID module, or the Kodak video camera. (Tr. p. 46)

14. The Zyco controller captures the signals that are generated between the control handle and the 35 millimeter camera in order to synchronize the freeze frame equipment with the 35 millimeter camera. (Tr. p. 46)

15. The Zyco controller synchronizes the shutter mechanism on the traditional camera with the freeze frame equipment so that the traditional camera and the freeze

frame equipment take the same picture at the same time. Without synchronization, there could be discrepancies between the two pictures. (Taxpayer Ex. #7; Tr. pp. 18-19, 48-49)

16. The Zyco controller tells the Kodak 4000 CCD video camera when to shift into “flash acquired mode,” which means that the video camera adjusts itself for the intense bright light that goes off with the flash. The Zyco controller tells the video camera when to electronically acquire the image. (Tr. pp. 49-53)

17. The Kodak 4000 CCD video camera produces an analog signal that is transmitted to the NCR computer, which processes the signal to create a digital image. The video camera acquires the data and transfers it to the NCR computer; it captures an image and sends the data signals to the NCR computer. The video camera does not use any film. (Taxpayer Ex. #2, 4; Tr. pp. 15-16, 44, 56)

18. The video camera captures the same image as the 35 millimeter camera, except electronically instead of chemically. Both the video camera and the 35 millimeter camera serve the same purpose. (Tr. p. 42)

19. The Tonkina lens is attached to the video camera. It sizes and focuses the image that is being acquired; it allows the image to pass to the Kodak video camera. (Taxpayer Ex. #5; Tr. pp. 15-17, 43-44)

20. The lens on the video camera serves the same purpose as the lens on the 35 millimeter camera. (Tr. p. 43)

21. The NCR computer serves two functions: one is to compile the customer’s information file (a/k/a computer or film file); the other is to create the digital image file. (Tr. pp. 21,56,67)

22. The computer file is established when a customer arrives in the sitting room and the photographer types information relating to the customer into the NCR computer. The file includes information such as the customer's name, the sitting number, the photographer's code, the studio number, the camera room, the emulsion number, and the type of film. In addition, once a negative is exposed and a digital image is created, a "record" for that image is added to the computer file. (Taxpayer Ex. #9,10,13; Tr. pp. 21-22, 27, 31-32, 57)

23. The second process performed by the NCR computer is the creation of the digital image file. Once the photographer presses the trip button, the Kodak video camera produces an analog signal that is sent to the NCR computer. The computer immediately converts the analog signal to digital format to create the digital image file. The digital image is displayed on the NCR monitor. The monitor is the tool that is necessary to view the image. (Taxpayer Ex. #9,10; Tr. pp. 20-24, 56-58, 64)

24. For each customer, there is one computer file and several digital image files. For each digital image file, there is a corresponding negative in the 35 millimeter camera. Every time the 35 millimeter camera exposes a negative (which is the same time that a digital image is created), a new "record" is added to the computer file. In other words there is one record for each digital image. (Taxpayer Ex. #9, 10, 13; Tr. pp. 21-22, 27, 31-32, 56-57)

25. During Stage 1 of the process, the customer looks at the digital image on the NCR monitor and decides whether it is acceptable or not. If the image is acceptable, then nothing is added to the computer file. If the image is not acceptable to the customer (e.g., the customer's eyes are closed in the picture), then the photographer "deselects" the

image. This means that the photographer types information into the computer file to indicate that the negative relating to that image should not be developed for that customer. During the “deselection process, the image is not deleted. (Tr. pp. 22-24)

26. The computer file and the digital image files are initially saved to the hard drive of the NCR computer. (Tr. p. 58)

27. The Zyco ID Module identifies the film that is in the 35 millimeter camera. The ID Module has internal hardware known as light emitting diodes (“LED’s”) that distribute a sequence of numbers onto the film. The numbers are used for tracking the production of the film. The numbers show the same information that is in the computer file (i.e., the customer’s sitting information) on the film in the 35 millimeter camera. (Taxpayer Ex. #8; Tr. pp. 19-20, 54)

28. The primary function of the ID Module is to put identification information onto the film. This information also serves as a backup to the information in the computer file. (Tr. pp. 54-55)

29. After the photographer finishes taking the pictures during Stage 1, the computer file and the image files are sent from the NCR computer to the Pentium computer. The Pentium computer is located outside of the sitting room. (Tr. pp. 27-28)

30. “Stage 2” of the process begins after the files are sent to the Pentium computer. The items used in Stage 2 are the Pentium computer, a monitor, and the Sony printer. (Taxpayer Ex. #2; Tr. pp. 14, 27-28, 33, 40)

31. Once the files are transferred to the Pentium computer, they are deleted from the NCR computer so that there is plenty of storage space on the NCR computer for the next customer. (Tr. p. 58)

32. During Stage 2, the photographer and the customer look at the images that were accepted in Stage 1. At this time the customer decides (1) which, if any, negatives should be developed, and (2) which, if any, of the freeze frame products the customer would like to purchase. (Tr. pp. 28, 60-61)

33. There are two types of products that are produced by the freeze frame equipment: (1) proof sheets and (2) portrait creations. (Taxpayer Ex. #12, 17, 18; Tr. pp. 33-36)

34. A proof sheet is the digital images on paper. It is an example of what the developed negatives will look like. It is printed within minutes of the sitting. The customer can take the proof sheet home on the day of the sitting. (Taxpayer Ex. #12, 17; Tr. pp. 33-36)

35. A portrait creation is one or more of the digital images on paper with various embellishments, such as colorful items or words placed around the images. In order to make the portrait creation, the Pentium computer overlays the images onto various templates. This is processed by the Sony printer. Like the proof sheet, it is available to the customer within minutes and can be taken home with them. (Taxpayer Ex. #12, 18; Tr. pp. 33-36)

36. The freeze frame products are not produced on a speculative basis. In other words, the freeze frame products are not produced until the customer decides to purchase one. (Tr. p. 83)

37. The primary function of the Pentium computer is to rearrange and prorate the digital images so that they may be printed out on the paper. The Pentium computer performs functions that are more demanding than the functions performed by the NCR

computer. The Pentium computer changes the size of the images and maneuvers them so that they fit on the page. (Tr. pp. 61-63)

38. The primary function of the Sony printer is to produce high-quality color images for the customer. The printer transposes the digital images onto paper. (Tr. p. 33)

39. The analog signal from the video camera must be converted to a digital format before the printer can print the proof sheet or portrait creation. (Tr. p. 59)

40. During Stage 2, the photographer and the customer “add content” to the computer file. This means that for each image shown on the monitor, the customer selects the quantity and size of the portrait to be developed at the processing facility. This information is added to the records in the computer file. The records, which each link to a negative, are updated with this information during this stage. (Tr. pp. 28-29, 40, 60-62)

41. After a customer has completed the process of selecting the portraits to be developed, the information in the computer file is transferred electronically, via modem to the central processing facility. (Tr. p. 32)

42. The information from the computer file, along with the corresponding information that is put on the film by the Zyco ID Module, is used at the central processing facility to determine which negatives are to be developed for the customer. (Tr. pp. 20, 31-33, 54-55)

43. As a negative advances through a printer at the processing plant, the negative is linked to one of the records in the computer file. Based on the record in the computer file, the computer system dictates to the printer whether or not to print a negative and what size should be printed. (Tr. p. 32)

44. Sometimes after the computer file is sent to the central processing plant a customer will decide to order more pictures or have a specific negative developed. When that happens, usually someone will manually scroll through the film to determine which negative to print. The information that is put on the film by the Zyco ID Module is used to determine which negative to print. (Tr. p. 55)

45. Prior to the use of the freeze frame equipment, the film from the 35 millimeter camera was sent to the processing plant where it was taken to an editing station. At the station, an editor would review the negatives and decide whether they should be developed for the customer. (Taxpayer Ex. #15, 16; Tr. pp. 24-26)

46. Under the traditional method, the customer was not able to select which negatives should be developed. (Tr. pp. 29-30)

47. The taxpayer pays retailers' occupation tax on the sale of the freeze frame products. (Tr. pp. 5, 84)

48. The customer pays a session fee in addition to the purchase of the products. (Tr. p. 80)

49. During the first half of fiscal year 1997, 63.6% of the taxpayer's customers purchased one or both of the freeze frame products. This was an increase from 59.5% for the first half of fiscal year 1996. (Taxpayer Ex. #19; Tr. pp. 80-81)

50. As the quality of the freeze frame products has improved over the years, more customers have purchased the products. (Tr. p. 81)

51. During the first half of fiscal year 1997, 10.8% of the taxpayer's revenues were from the sale of freeze frame products. This increased from 9.6% for the first half of fiscal year 1996. (Taxpayer Ex. #19; Tr. p. 82)

52. During the first half of fiscal year 1997, the average customer spent \$53.20 on traditional portraits and \$5.75 on freeze frame products. (Taxpayer Ex. #19; Tr. p. 82)

53. The taxpayer did not present information concerning the number of customers who bought the freeze frame products during the audit period.

54. The taxpayer did not present documentary evidence indicating that some of the Zyco Controllers listed in the audit report are actually Zyco ID Modules.

55. Department audited the taxpayer for the time periods of July 1, 1991 to November 30, 1993 and December 1, 1993 to December 31, 1994. (Dept. Group Ex. #1)

56. On February 21, 1996, the Department prepared corrected tax returns for the audit periods in question. For the first audit period, the return shows total tax due in the amount of \$58,400. The corrected return for the second audit period shows a total tax liability of \$19,366 plus a late filing penalty of \$521. A copy of the corrected returns was admitted into evidence under the certificate of the Director of the Department. (Dept. Group Ex. #1)

58. On June 18, 1997, the Department issued a Notice of Tentative Denial of Claim, which denied the taxpayer's total claim in the amount of \$99,721.¹ A copy of the Notice of Tentative Denial of Claim was allowed into evidence under the certificate of the Director of the Department. (Dept. Group Ex. #1)

CONCLUSIONS OF LAW

The ALJ concluded that certain equipment used in digital photography applications is exempt from tax because it qualifies as equipment used in photoprocessing. An examination of the definition of "photoprocessing" and the

¹ At the conclusion of the audit, the Department determined that the taxpayer overpaid a portion of its retailer's occupation tax liability. (Tr. p.5) The overpayment was offset against the use tax liability, and the net amount was included in the NTLs. The amount of the claim relates solely to the freeze frame equipment.

exemption for photoprocessing machinery and equipment contained in the Use Tax Act (35 ILCS 105/3-3 and 105/3-15) does not support the ALJ's conclusion. The current statute is not broad enough to encompass digital photography. Section 3 of the Use Tax [35 ILCS 105/3-3] subjects the products of photoprocessing to tax and states as follows:

A tax is imposed upon the privilege of using in this State, tangible personal property purchased at retail from a retailer, including computer software, *and including photographs, negatives, and positives that are the product of photoprocessing*, but not including products of photoprocessing produced for use in motion pictures for commercial exhibition. (Emphasis added)

Section 3-15 of the Use Tax Act sets forth the statutory definition of photoprocessing:

For purposes of the tax imposed on photographs, negatives, and positives by this Act, "photoprocessing" includes, but is not limited to, developing films, positives, negatives, and transparencies, and tinting, coloring, making, and enlarging prints.

Section 3-5 of the Use Tax Act [35 ILCS 105/3-5] provides an exemption from tax for:

Photoprocessing machinery and equipment, including repair and replacement parts, both new and used, including that manufactured on special order, certified by the purchaser to be *used primarily for photoprocessing*, and including photoprocessing machinery and equipment purchased for lease. (Emphasis added)

It is clear from the plain language of the Use Tax Act that digital photography is not "photoprocessing" as that term is defined in the Use Tax Act. Therefore, machinery and equipment used in digital photography does not qualify for the photoprocessing machinery and equipment exemption from the Use Tax Act. With all due respect to the administrative law judge, I am unable to agree with her conclusion that the language in the definition of photoprocessing that states that the definition is "not limited to" the specifically enumerated items is sufficiently broad to include digital photography. The "but is not limited to" language is designed to allow inclusion of photoprocessing activities that are of a similar nature to those specifically listed. Digital photography is not of a similar nature to traditional photoprocessing.

I do not agree with the conclusion of the administrative law judge that the law, as written, authorizes the recommendation for disposition in this case. I have a fundamental difficulty with adopting an Administrative Hearing decision that attempts to “correct” or “expand” a statute to take into account changes in technology that have occurred since the original enactment of the statute. What I would be doing by adopting this recommendation for disposition is changing the scope of the statute. Such changes are more properly the province of the Illinois General Assembly.

In addition, although not stated in the recommendation for disposition, the recommended disposition is directly contrary to written statements of the Department made in letter rulings. I take official notice of these ruling letters. The Department, through the Legal Services Office, has stated in a number of letter rulings that the sale of digital photography is not the sale of products of photoprocessing. In addition, the rulings have referred taxpayers to the Service Occupation Tax for the tax treatment of the service of digital photography. (See ST 98-103-GIL, ST 98-0119-GIL, ST 98-0215-GIL, ST 98-0328-GIL)

I am mindful of the fact that it may be argued that as a technical proposition, general information letters are not binding on the Department and as a result it does not matter whether the Department has taken a position on digital photography in letter rulings. [2 Ill. Adm. Code 1200.120] However, although general information letters are not binding, they are instructive. It would be unfair to taxpayers to take one position in general information letters and take a contrary position in administrative hearing. The Legal Services Office should have proposed an administrative rule to set forth the Department’s determination that the sale of digital photography is not a sale of the products of photoprocessing for purposes of taxation under the Use Tax Act. Section 3 of the Illinois Department of Revenue Sunshine Act requires the Department to propose rulemaking whenever a letter ruling contains any policy of general applicability. [20 ILCS 2515/3] I have instructed the Legal Services Office to develop a rulemaking to address this policy.

On the basis of the above, it is my determination as Director that the recommendation of the administrative law judge regarding the disposition of this case is rejected as inconsistent with prevailing law. It is therefore order that the Notices of Tax

Liability shall be affirmed and the Claim for Credit or Refund shall be denied and that a final assessment issue forthwith.

Glen L. Bower
Director of Revenue

ST 99-9

Tax Type: ROT

Issue: Machinery & Equipment Exemption (Photoprocessing)

**STATE OF ILLINOIS
DEPARTMENT OF REVENUE
OFFICE OF ADMINISTRATIVE HEARINGS
SPRINGFIELD, ILLINOIS**

THE DEPARTMENT OF REVENUE)	
OF THE STATE OF ILLINOIS)	
)	Docket No. 96-ST-
v.)	IBT # 0
)	NTL #
TAXPAYER, INC.)	NTL #
Taxpayer)	Claim for Credit or Refund

RECOMMENDATION FOR DISPOSITION

Appearances: Charles Hickman, Special Assistant Attorney General, for the Department of Revenue of the State of Illinois; Amy M. Faber and Lewis Striebeck of The Stolar Partnership for TAXPAYER, Inc.

Synopsis:

This case concerns whether equipment that processes and produces digital images qualifies for the photoprocessing exemption under the Use Tax Act (35 ILCS 105/1 *et seq.*). The Department of Revenue (“Department”) conducted an audit of TAXPAYER, Inc. (“taxpayer”) for the time periods of July 1, 1991 to November 30, 1993 and December 1, 1993 to December 31, 1994 and concluded that the taxpayer owed additional tax on various items. The Department issued two Notices of Tax Liability (NTLs), which the taxpayer timely protested. The taxpayer subsequently paid the tax and filed a Claim for Credit or Refund, which was denied by the Department. The taxpayer’s

protest of the Department's Notice of Tentative Denial of Claim was consolidated with the present case. An evidentiary hearing was held during which the taxpayer argued that use tax is not owed on the following equipment because the items qualify for the photoprocessing exemption or, in the alternative, the manufacturing machinery and equipment exemption:²

- (1) Kodak 4000 CCD video camera;
- (2) Tonkina lens;
- (3) base power supply (a/k/a freeze frame power supply);
- (4) Zyco controller;
- (5) Zyco ID Module;
- (6) NCR computer;
- (7) NCR monitor;
- (8) Pentium computer;
- (9) Sony printer.

After reviewing the record, it is recommended that this matter be resolved partially in favor of the taxpayer and partially in favor of the Department.

FINDINGS OF FACT:

1. The taxpayer's equipment is used at various portrait studios, such as SMILING PRETTY STUDIO in FICTITIOUS CITY, Illinois. (Tr. pp. 39-40, 71-72)

2. When customers arrive at the portrait studios to have their picture taken, they are escorted into a sitting room. The equipment that is at issue is located in this room, except for the Pentium computer and the Sony printer. The operations that take place in this room are known as "Stage 1" of the process. (Taxpayer Ex. #2; Tr. pp. 14, 57)

3. Once a customer is in the sitting room, the photographer sets up an information file (a/k/a a computer file or film file) for the customer. The photographer creates this file by typing certain information (e.g., the customer's name, the photographer's code, the studio number and sitting number) into the NCR computer. (Tr. pp. 21-22, 56-57)

² These exemptions are found at 35 ILCS 105/3-5(15) and 35 ILCS 105/3-5(18).

4. When the customer poses for a picture, the photographer presses a “trip button,” which is located on a hand-held device called the control handle. Once the trip button is pressed, this triggers two separate but simultaneous methods for taking the customer’s picture. One method is referred to by the taxpayer as the “traditional” method; the other is the “freeze frame” method. Even though the two methods are separate, they are set up so that they simultaneously take the same picture of the customer. (Tr. pp. 49-53)

5. Under the traditional method, a 35 millimeter camera is used to take a picture of the customer. When the photographer presses the trip button, this sends a signal to the “base power supply” (a/k/a the freeze frame power supply), which then sends a signal two ways at the same time: one signal tells the 35 millimeter camera to open the shutter to expose the film, the other signal goes to the freeze frame equipment. (Tr. pp. 13, 49-53)

6. Under the traditional method, the 35 millimeter camera captures an image onto its film. When the silver salts emulsion film is exposed, it captures light data chemically. The exposed film from the camera is subsequently sent to a plant in St. Louis, Missouri for processing. (Tr. pp. 42-44, 59)

7. Under the freeze frame method, equipment is used to process digital images, and a heat offset printer produces pictures of the digital images within minutes after the photographer presses the trip button. (Tr. pp. 13, 75-76)

8. Under the freeze frame method, the pressing of the trip button sends a signal to the base power supply, which sends a signal to the Zyco controller. The Zyco controller tells the Kodak 4000 CCD video camera (“video camera”) to acquire an image. This

happens at the exact same time that the base power supply tells the 35 millimeter camera to open the shutter. (Tr. pp. 49-53)

9. The base power supply provides power to various items of the whole system. It was designed to interface with the freeze frame equipment. The base power supply receives current from a source such as a wall outlet and converts some of it to direct current; it redistributes the power, sometimes at lower voltages for some of the equipment. (Taxpayer Ex. #6; Tr. pp. 17-18, 45-48)

10. The base power supply also generates a signal to the equipment to discharge the strobe or the flash tubes when the shutter of the 35 millimeter camera opens. (Tr. pp. 47-48)

11. The base power supply provides power to the control handle and the 35 millimeter camera. It also powers a black and white video camera and the motors that are used to position the camera system. The black and white video camera is used to ensure that the customer is in the proper position. None of these items are at issue in this case. (Tr. pp. 17-18, 45-48)

12. Prior to the installation of the freeze frame equipment, there was a power supply that received a signal from the control handle and sent a signal to the 35 millimeter camera to trip the shutter. It also powered the motors and the black and white video camera. This power supply did not interface with freeze frame equipment. (Taxpayer Ex. #6; Tr. pp. 17-18, 45-48, 51)

13. The base power supply does not power the Zyco controller, the Zyco ID module, or the Kodak video camera. (Tr. p. 46)

14. The Zyco controller captures the signals that are generated between the control handle and the 35 millimeter camera in order to synchronize the freeze frame equipment with the 35 millimeter camera. (Tr. p. 46)

15. The Zyco controller synchronizes the shutter mechanism on the traditional camera with the freeze frame equipment so that the traditional camera and the freeze frame equipment take the same picture at the same time. Without synchronization, there could be discrepancies between the two pictures. (Taxpayer Ex. #7; Tr. pp. 18-19, 48-49)

16. The Zyco controller tells the Kodak 4000 CCD video camera when to shift into “flash acquired mode,” which means that the video camera adjusts itself for the intense bright light that goes off with the flash. The Zyco controller tells the video camera when to electronically acquire the image. (Tr. pp. 49-53)

17. The Kodak 4000 CCD video camera produces an analog signal that is transmitted to the NCR computer, which processes the signal to create a digital image. The video camera acquires the data and transfers it to the NCR computer; it captures an image and sends the data signals to the NCR computer. The video camera does not use any film. (Taxpayer Ex. #2, 4; Tr. pp. 15-16, 44, 56)

18. The video camera captures the same image as the 35 millimeter camera, except electronically instead of chemically. Both the video camera and the 35 millimeter camera serve the same purpose. (Tr. p. 42)

19. The Tonkina lens is attached to the video camera. It sizes and focuses the image that is being acquired; it allows the image to pass to the Kodak video camera. (Taxpayer Ex. #5; Tr. pp. 15-17, 43-44)

20. The lens on the video camera serves the same purpose as the lens on the 35 millimeter camera. (Tr. p. 43)

21. The NCR computer serves two functions: one is to compile the customer's information file (a/k/a computer or film file); the other is to create the digital image file. (Tr. pp. 21, 56, 67)

22. The computer file is established when a customer arrives in the sitting room and the photographer types information relating to the customer into the NCR computer. The file includes information such as the customer's name, the sitting number, the photographer's code, the studio number, the camera room, the emulsion number, and the type of film. In addition, once a negative is exposed and a digital image is created, a "record" for that image is added to the computer file. (Taxpayer Ex. #9, 10, 13; Tr. pp. 21-22, 27, 31-32, 57)

23. The second process performed by the NCR computer is the creation of the digital image file. Once the photographer presses the trip button, the Kodak video camera produces an analog signal that is sent to the NCR computer. The computer immediately converts the analog signal to a digital format to create the digital image file. The digital image is displayed on the NCR monitor. The monitor is the tool that is necessary to view the image. (Taxpayer Ex. #9, 10; Tr. pp. 20-24, 56-58, 64)

24. For each customer, there is one computer file and several digital image files. For each digital image file, there is a corresponding negative in the 35 millimeter camera. Every time the 35 millimeter camera exposes a negative (which is the same time that a digital image is created), a new "record" is added to the computer file. In other words

there is one record for each digital image. (Taxpayer Ex. #9, 10, 13; Tr. pp. 21-22, 27, 31-32, 56-57)

25. During Stage 1 of the process, the customer looks at the digital image on the NCR monitor and decides whether it is acceptable or not. If the image is acceptable, then nothing is added to the computer file. If the image is not acceptable to the customer (e.g., the customer's eyes are closed in the picture), then the photographer "deselects" the image. This means that the photographer types information into the computer file to indicate that the negative relating to that image should not be developed for that customer. During the "deselection" process, the image is not deleted. (Tr. pp. 22-24)

26. The computer file and the digital image files are initially saved to the hard drive of the NCR computer. (Tr. p. 58)

27. The Zyco ID Module identifies the film that is in the 35 millimeter camera. The ID Module has internal hardware known as light emitting diodes ("LED's") that distribute a sequence of numbers onto the film. The numbers are used for tracking the production of the film. The numbers show the same information that is in the computer file (i.e., the customer's sitting information) on the film in the 35 millimeter camera. (Taxpayer Ex. #8; Tr. pp. 19-20, 54)

28. The primary function of the ID Module is to put identification information onto the film. This information also serves as a backup to the information in the computer file. (Tr. pp. 54-55)

29. After the photographer finishes taking the pictures during Stage 1, the computer file and the image files are sent from the NCR computer to the Pentium computer. The Pentium computer is located outside of the sitting room. (Tr. pp. 27-28)

30. "Stage 2" of the process begins after the files are sent to the Pentium computer. The items used in Stage 2 are the Pentium computer, a monitor, and the Sony printer. (Taxpayer Ex. #2; Tr. pp. 14, 27-28, 33, 40)

31. Once the files are transferred to the Pentium computer, they are deleted from the NCR computer so that there is plenty of storage space on the NCR computer for the next customer. (Tr. p. 58)

32. During Stage 2, the photographer and customer look at the images that were accepted in Stage 1. At this time, the customer decides (1) which, if any, negatives should be developed, and (2) which, if any, of the freeze frame products the customer would like to purchase. (Tr. pp. 28, 60-61)

33. There are two types of products that are produced by the freeze frame equipment: (1) proof sheets and (2) portrait creations. (Taxpayer Ex. #12, 17, 18; Tr. pp. 33-36)

34. A proof sheet is the digital images on paper. It is an example of what the developed negatives will look like. It is printed within minutes of the sitting. The customer can take the proof sheet home on the day of the sitting. (Taxpayer Ex. #12, 17; Tr. pp. 33-36)

35. A portrait creation is one or more of the digital images on paper with various embellishments, such as colorful items or words placed around the images. In order to make the portrait creation, the Pentium computer overlays the images onto various templates. This is processed by the Sony printer. Like the proof sheet, it is available to the customer within minutes and can be taken home with them. (Taxpayer Ex. #12, 18; Tr. pp. 33-36)

36. The freeze frame products are not produced on a speculative basis. In other words, the freeze frame products are not produced until the customer decides to purchase one. (Tr. p. 83)

37. The primary function of the Pentium computer is to rearrange and prorate the digital images so that they may be printed out on the paper. The Pentium computer performs functions that are more demanding than the functions performed by the NCR computer. The Pentium computer changes the size of the images and maneuvers them so that they fit on the page. (Tr. pp. 61-63)

38. The primary function of the Sony printer is to produce high-quality color images for the customer. The printer transposes the digital images onto paper. (Tr. p. 33)

39. The analog signal from the video camera must be converted to a digital format before the printer can print the proof sheet or portrait creation. (Tr. p. 59)

40. During Stage 2, the photographer and the customer “add content” to the computer file. This means that for each image shown on the monitor, the customer selects the quantity and size of the portrait to be developed at the processing facility. This information is added to the records in the computer file. The records, which each link to a negative, are updated with this information during this stage. (Tr. pp. 28-29, 40, 60-62)

41. After a customer has completed the process of selecting the portraits to be developed, the information in the computer file is transferred electronically, via modem, to the central processing facility. (Tr. p. 32)

42. The information from the computer file, along with the corresponding information that is put on the film by the Zyco ID Module, is used at the central

processing facility to determine which negatives are to be developed for the customer.
(Tr. pp. 20, 31-33, 54-55)

43. As a negative advances through a printer at the processing plant, the negative is linked to one of the records in the computer file. Based on the record in the computer file, the computer system dictates to the printer whether or not to print a negative and what size should be printed. (Tr. p. 32)

44. Sometimes after the computer file is sent to the central processing plant a customer will decide to order more pictures or have a specific negative developed. When that happens, usually someone will manually scroll through the film to determine which negative to print. The information that is put on the film by the Zyco ID Module is used to determine which negative to print. (Tr. p. 55)

45. Prior to the use of the freeze frame equipment, the film from the 35 millimeter camera was sent to the processing plant where it was taken to an editing station. At the station, an editor would review the negatives and decide whether they should be developed for the customer. (Taxpayer Ex. #15, 16; Tr. pp. 24-26)

46. Under the traditional method, the customer was not able to select which negatives should be developed. (Tr. pp. 29-30)

47. The taxpayer pays retailers' occupation tax on the sale of the freeze frame products. (Tr. pp. 5, 84)

48. The customer pays a session fee in addition to the purchase of the products.
(Tr. p. 80)

49. During the first half of fiscal year 1997, 63.6% of the taxpayer's customers purchased one or both of the freeze frame products. This was an increase from 59.5% for the first half of fiscal year 1996. (Taxpayer Ex. #19; Tr. pp. 80-81)

50. As the quality of the freeze frame products has improved over the years, more customers have purchased the products. (Tr. p. 81)

51. During the first half of fiscal year 1997, 10.8% of the taxpayer's revenues were from the sale of freeze frame products. This increased from 9.6% for the first half of fiscal year 1996. (Taxpayer Ex. #19; Tr. p. 82)

52. During the first half of fiscal year 1997, the average customer spent \$53.20 on traditional portraits and \$5.75 on freeze frame products. (Taxpayer Ex. #19; Tr. p. 82)

53. The taxpayer did not present information concerning the number of customers who bought the freeze frame products during the audit period.

54. The taxpayer did not present documentary evidence indicating that some of the Zyco Controllers listed in the audit report are actually Zyco ID Modules.

55. Department audited the taxpayer for the time periods of July 1, 1991 to November 30, 1993 and December 1, 1993 to December 31, 1994. (Dept. Group Ex. #1)

56. On February 21, 1996, the Department prepared corrected tax returns for the audit periods in question. For the first audit period, the return shows total tax due in the amount of \$58,400. The corrected return for the second audit period shows a total tax liability of \$19,366 plus a late filing penalty of \$521. A copy of the corrected returns was admitted into evidence under the certificate of the Director of the Department. (Dept. Group Ex. #1)

57. The taxpayer paid the tax that the Department determined was owed as a result of the audit and on April 17, 1997 filed a Claim for Credit or Refund. (Dept. Group Ex. #1)

58. On June 18, 1997, the Department issued a Notice of Tentative Denial of Claim, which denied the taxpayer's total claim in the amount of \$99,721.³ A copy of the Notice of Tentative Denial of Claim was allowed into evidence under the certificate of the Director of the Department. (Dept. Group Ex. #1)

CONCLUSIONS OF LAW:

The Use Tax Act ("Act") imposes a tax upon the privilege of using in Illinois tangible personal property purchased at retail from a retailer. 35 ILCS 105/3. Section 12 of the Use Tax Act incorporates by reference sections 4 and 5 of the Retailers' Occupation Tax Act ("ROTA") (35 ILCS 120/1 *et seq.*), which provide that the corrected return issued by the Department is *prima facie* correct and is *prima facie* evidence of the correctness of the amount of tax due, as shown therein. 35 ILCS 105/12; 120/4, 5. Section 12 also incorporates section 6b of the ROTA, which provides that the Department's Notice of Tentative Denial of Claim constitutes *prima facie* proof of the correctness of the Department's determination, as shown therein. 35 ILCS 105/12; 120/6b.

Once the Department has established its *prima facie* case by submitting a certified copy of the corrected return and Notice of Tentative Denial of Claim into evidence, the burden shifts to the taxpayer to overcome this presumption of validity. Clark Oil & Refining Corp. v. Johnson, 154 Ill.App.3d 773, 783 (1st Dist. 1987). To prove its case, a taxpayer must present more than its testimony denying the Department's assessment.

³ At the conclusion of the audit, the Department determined that the taxpayer overpaid a portion of its retailers' occupation tax liability. (Tr. p. 5) The overpayment was offset against the use tax liability, and the net amount was included in the NTLs. The amount of the claim relates solely to the freeze frame equipment.

Sprague v. Johnson, 195 Ill.App.3d 798, 804 (4th Dist. 1990). The taxpayer must present sufficient documentary evidence to support its claim. Id.

Use in Connection with Traditional Method

The taxpayer's first argument is that the equipment qualifies for the photoprocessing exemption because it is used in connection with the editing, numbering, and production control functions that are necessary to develop the traditional photographs. Section 3-5 of the Act provides that the following tangible personal property is exempt from tax:

“Photoprocessing machinery and equipment, including repair and replacement parts, both new and used, including that manufactured on special order, certified by the purchaser to be used **primarily** for photoprocessing, and including photoprocessing machinery and equipment purchased for lease. (35 ILCS 105/3-5(15)) (emphasis added)

It is well settled that tax exemption provisions are strictly construed in favor of taxation. Heller v. Fergus Ford, Inc., 59 Ill.2d 576, 579 (1975). The party claiming the exemption has the burden of clearly proving that it is entitled to the exemption, and all doubts are resolved in favor of taxation. Id.

The taxpayer claims that all of the items are exempt under this section because they are used to determine which one or more of the negatives from the 35 millimeter camera should be developed into the traditional photographs. The taxpayer states that before it started using the freeze frame equipment, an employee at the processing plant would determine which negatives should be developed for the customer. The customer had no idea what the photographs would look like until they were developed at the processing plant and sent back to the customer. The selection of which negatives to develop was totally within the discretion of the “editors” at the plant. Once the

photographs were sent to the customer, the customer would then decide whether or not to buy them and whether or not a certain picture should be developed into a different size.

With the use of the freeze frame equipment, the “editing” functions that previously were performed at the processing plant have been greatly reduced, along with the amount of waste that was involved with the production of the traditional photographs. The freeze frame equipment is used to let the customer select at the time of the sitting which negative from the 35 millimeter camera should be developed. The customer also decides the size and quantity of the photos. This is done during Stage 2 of the process. The information that is put into the computer file during Stage 2 is used to determine the size and number of photographs to be developed.

The Department contends that the primary function of the equipment is “pre-production marketing,” and therefore it does not qualify under this section. The Department claims that the equipment does not perform “editing” functions as the taxpayer claims, but simply allows the customers to view the poses and therefore serves as a pre-production marketing device. In addition, the Department argues that the taxpayer did not present evidence showing what percentage of the time the computers are used on the image production functions versus the “editing” functions, and therefore the taxpayer has failed to produce sufficient evidence to show the primary purpose of the equipment.

In response, the taxpayer argues that while some marketing goals may be furthered by the equipment’s ability to allow the customers to participate in the editing process, this is incidental to the process for which the equipment is used. The taxpayer states that because all of the freeze frame equipment is used continuously and

simultaneously for both the editing functions and the production of the proof sheets and portrait creations, it is exempt.

The photoprocessing exemption applies to machinery and equipment used “primarily” for photoprocessing. (35 ILCS 105/3-5(15)) It is therefore necessary to determine the primary purpose of the equipment in order to decide whether the equipment is exempt. The purchaser of the items must establish that the machinery or equipment is used over 50 percent in an exempt manner in order to claim the deduction. (86 Ill.Admin.Code, ch. 1, §130.330(d)(1)) All doubts concerning the primary purpose of the equipment must be resolved in favor of taxation. Heller at 579.

The taxpayer has presented sufficient evidence to show that the Zyco ID Module is exempt under this section. The primary purpose of the ID Module is to put identification information on the film in the 35 millimeter camera. The numbers that are put on the film are used in connection with the computer file to determine which negatives should be developed. The numbers are used to track the production of the conventional photographs and work as an indexing system for the negatives. The functions performed by the ID Module seem to be similar to a “film indexer,” which is listed in the Department’s regulation as an example of the type of equipment that is exempt under this section. (See 86 Ill.Admin.Code ch. 1, §130.330(b)(9)) Because the primary purpose of the ID Module is to identify the film in order to aid the development of the conventional photographs, it is exempt.

The taxpayer has failed to present sufficient evidence to show that the primary purpose of the remaining items is to assist the traditional photoprocessing method. The taxpayer admits that the equipment is used continuously and simultaneously for both the

“editing” of the traditional photos and the production of the freeze frame products. The fact that the equipment serves two purposes makes it difficult to distinguish the primary purpose. The taxpayer indicated that as the quality of the freeze frame products has improved over the years, more customers have purchased them. During the first half of fiscal year 1997, 63.6% of the customers purchased one or both of the freeze frame products and 10.8% of the company’s revenues were attributed to the new products. Nevertheless, the taxpayer did not provide any evidence showing what the equipment was primarily used for during the audit period. Because the record is unclear as to whether the equipment was used more than 50% to assist in deciding which negatives to develop and all doubts must be resolved in favor of taxation, the taxpayer has failed to meet its burden on this issue.

Whether the Freeze Frame Method is Photoprocessing

Next, the taxpayer argues that all of the freeze frame items are exempt because the freeze frame method is, in and of itself, “photoprocessing” within the meaning of the Act. Section 3-15 of the Act provides in relevant part as follows:

“For purposes of the tax imposed on photographs, negatives, and positives by this Act, ‘photoprocessing’ **includes, but is not limited to**, developing films, positives, negatives, and transparencies, and tinting, coloring, making, and enlarging prints. Photoprocessing does not include color separation, typesetting, and platemaking by photographic means in the graphic arts industry and does not include any procedure, process, or activity connected with the creation of the images on the film from which the negatives, positives, or photographs are derived. * * *” (35 ILCS 105/3-15) (emphasis added)

The Department argues that under this section the word “photoprocessing” refers only to the conventional method of developing photographs and therefore the legislature intended only to exempt equipment that is used to develop the traditional photographs. Because the digital image processing equipment does not use film, negatives or positives and is

not used to develop conventional photographs, the Department claims that it is not exempt.

The primary rule of statutory construction is to ascertain and give effect to the intention of the legislature. Board of Trustees of Southern Illinois University v. Department of Human Rights, 159 Ill.2d 206, 211 (1994). In order to determine the legislature's intent, the first step is to consider the plain and ordinary meaning of the language of the statute. Thomas v. Greer, 143 Ill.2d 271, 278 (1991).

The Department argues that “photoprocessing” means the development of photographs through the use of chemical film. The Department cites the 1991 edition of the Encyclopaedia Britannica, which defines photography as the process of producing an image by exposing silver salts emulsion coated film, developing the emulsion, and printing the image. The taxpayer argues that an analysis of the plain meaning of the word should not require resorting to an outdated technical explanation; it should involve an inquiry into the common understanding of the phrase.

The plain language of the statute indicates that the legislature did not intend to limit the meaning of the term “photoprocessing.” By using the words “includes, but is not limited to,” the legislature clearly intended the term “photoprocessing” to have a flexible meaning; the legislature envisioned that the scope of the term would change with technology. Digital technology is now used by the taxpayer to capture, store, and print images. The digital images produced by the taxpayer that are sold to customers (Exhibits #17 and 18) look like traditional photographs; it is difficult to discern a difference between the two different products. Once a customer purchases a digital image, it is often framed and referred to as a photograph just like conventional photographs.

Another rule of statutory construction is that statutes are to be interpreted in a manner consistent with the state of the law that exists at the time of the enactment of the statute. Illinois Bell Telephone Co. v. Allphin, 93 Ill.2d 241, 249 (1982). A review of the law as it existed at the time that the photoprocessing exemption was enacted reveals that the legislature intended to exempt equipment that is used to produce products that are sold by the photoprocessing industry.

Prior to the enactment of the photoprocessing exemption, the Illinois Supreme Court addressed the issue of whether photoprocessing equipment qualified for the manufacturing machinery and equipment exemption under the Use Tax Act. In Colorcraft Corporation, Inc. v. The Department of Revenue, 112 Ill.2d 473 (1986), the court determined that photoprocessing is properly classified as a service occupation rather than a manufacturing process. The court noted in an example that the products of photoprocessing are taxed at the service use tax rate rather than the use tax rate. Colorcraft at 480. Neither the Service Occupation Tax Act (“SOTA”) (35 ILCS 115/1 *et seq.*) nor the Service Use Tax Act (“SUT”) (35 ILCS 110/1 *et seq.*) have exemption provisions for manufacturing machinery and equipment as the ROTA and Use Tax Act do. The court therefore found that the equipment at issue in Colorcraft was not exempt from taxation.

After the Colorcraft decision, the General Assembly revised section 3 of the Use Tax Act, which states that the tax is imposed on the privilege of using in Illinois “tangible personal property purchased at retail from a retailer, * * * including photographs, negatives, and positives that are the product of photoprocessing, * * *.” 35 ILCS 105/3. A similar provision was added to the ROTA. (See 35 ILCS 120/2) In addition, the

General Assembly added a provision to both the ROTA and the Use Tax Act that exempts machinery and equipment used primarily for photoprocessing. (See 35 ILCS 120/2-5(20); 105/3-5(15)) Finally, the legislature included a section in both Acts that defines photoprocessing. (See 35 ILCS 120/2-15; 105/3-15)

As a result of these changes made by the General Assembly, the Department changed its regulations to include the following in its manufacturing machinery and equipment regulation under the ROTA:

“Effective September 1, 1988, **manufacturing includes photoprocessing if the products of photoprocessing are sold.** Machinery and equipment which would qualify for exemption includes, but are not limited to, developers, dryers, enlargers, mounting machines, roll film splicers, film developing image makers, disc film opening and spindling devices, film indexers, photographic paper exposure equipment, photographic paper developing machines, densitometers, print inspection devices, photo print/negative cut assembly stations, film sleeve insertion machines, negative image producers, film coating equipment, photo transparency mounters, processor rack sanitizers, photo print embossers, photo print mounting presses, graphic slide generators, chemical mixing equipment and paper exposure positioning and holding devices, etc. Cameras and equipment used to take pictures or expose film are not eligible as the photoprocessing begins after the film is exposed. Retail/net price calculation equipment and chemical reclamation equipment are not considered to be manufacturing machinery and equipment. (86 Ill.Admin.Code, ch. 1, §130.330(b)(9)) (emphasis added)

The Department also added the following to its regulation entitled “Persons Engaged in the Printing, Graphic Arts or Related Occupations, and Their Suppliers” under the ROTA:

“Effective September 1, 1988, **photographers, film makers, and other servicemen, are subject to Retailers’ Occupation Tax on the photoprocessing component of their total service charge when they sell products of photoprocessing.** The tax on the photoprocessing component will apply regardless of whether the photographer performs the photoprocessing in-house, or engages a third-party photoprocessor.” (86 Ill.Admin.Code, ch. 1, §130.2000(b)(3)) (emphasis added)

It is clear from these changes that the General Assembly intended to require photographers who are in the business of selling products of photoprocessing to remit ROT to the Department on the sale of those products. In addition to subjecting the products of photoprocessing to the ROT/UT rate, which is higher than the SOT/SUT rate, the legislature provided that the machinery and equipment that is primarily used to produce these products is exempt from taxation. In other words, after the Illinois Supreme Court determined that photoprocessing was not manufacturing but a service, the legislature enacted this change requiring the products of the photoprocessing industry to be taxed at the ROT/UT rate and allowing the equipment used to make the products to be exempt. The freeze frame products are products of the industry, and the taxpayer remits ROT on the sale of those products. Therefore, the equipment used to produce those products is exempt under the photoprocessing exemption.

This conclusion is further supported by the Department's assessment in this case. The taxpayer remits ROT on the sale of both the conventional photographs and the digital photographs. The Department does not contend that the taxpayer should not pay ROT on the sale of the freeze frame products. The Department does, however, argue that the production of digital images is not photoprocessing but rather a service, and therefore the equipment does not qualify for either the manufacturing machinery and equipment exemption or the photoprocessing exemption. The Department cites the Colorcraft case in support of this argument. This position, however, is inconsistent with the fact that the Department allows ROT to be charged on the sale of the freeze frame products. If this process of producing digital images is a service, then the Department should have

adjusted the assessment to show SOT rather than ROT on the sale of the freeze frame products.

The Department's last argument concerning statutory construction is that the doctrine of *ejusdem generis* should apply to the interpretation of "photoprocessing." Under this doctrine, when a statute provides a list of several things but states that the list is not exhaustive, then the class of unarticulated things are interpreted as those "others such like" the named items. Board of Trustees of Southern Illinois University at 211. The Department claims that the statute refers only to equipment that is used to process exposed silver salts emulsion film, and therefore the definition of photoprocessing that is proposed by the taxpayer is excluded. The taxpayer responds by stating that under the statute photoprocessing includes "making, and enlarging prints." (35 ILCS 105/3-15) The taxpayer correctly concludes that the digital image method is included in the list because it makes and enlarges prints. Therefore, the doctrine of *ejusdem generis* does not support the Department's position.

Exempt Equipment

The Department argues that even if digital image processing is photoprocessing within the meaning of the Act, the following items are not exempt because they perform "pre-processing" functions: (1) video camera; (2) lens; (3) base power supply; and (4) Zyco Controller.⁴ The Department contends that if digital technology is exempt, then the exemption should apply only to items that perform the functional equivalent of film development under the traditional method.

The taxpayer admits that some of the functions performed by the video camera and lens are similar to those performed by the 35 millimeter camera and lens. The

taxpayer argues, however, that the predominant functions performed by the freeze frame items is to instantaneously project the digitized images onto a viewing screen so that editing functions can be performed. The taxpayer states that these functions were traditionally performed after the film was sent to the central processing plant. Because the new technology allows the editing to be done at the time of the sitting, the taxpayer claims that this renders obsolete the regulation's premise that photoprocessing begins after the film is exposed.

Under the Act, photoprocessing does not include "any procedure, process, or activity connected with the creation of the images on the film from which the negatives, positives, or photographs are derived." (35 ILCS 105/3-15) The Department's regulation provides that "[c]ameras and equipment used to take pictures or expose film are not eligible as the photoprocessing begins after the film is exposed." (86 Ill.Admin.Code, ch. 1, §130.330(b)(9)) Even though the digital image processing equipment does not use film, the language of the statute indicates that the legislature intended to exclude equipment that is used to capture the images. Under the Act, photoprocessing does not begin until after the image is created. Thus, any equipment used in connection with the creation of the images does not qualify for the exemption.

In order to determine which items are exempt, it is necessary to once again focus on the primary purpose of the items. As previously stated, the owner of the equipment must establish that it is used over 50 percent in an exempt manner in order to claim the deduction. (86 Ill.Admin.Code, ch. 1, §130.330(d)(1)) "The fact that particular machinery or equipment may be considered essential to the conduct of the business of

⁴ The Department's argument that the Zyco ID Module also falls under this category is moot because the ID Module has already been found to be exempt.

manufacturing or assembling because its use is required by law or practical necessity does not, of itself, mean that machinery or equipment is used primarily in manufacturing or assembling.” (86 Ill.Admin.Code, ch. 1, §130.330(d)(2)) In other words, equipment that performs an ancillary or support role does not qualify for the exemption. All doubts concerning the primary purpose of the equipment must be resolved in favor of taxation. Heller at 579.

The evidence concerning the video camera, lens, base power supply, and Zyco controller does not support a finding that the items are used primarily for photoprocessing within the meaning of the Act. Photoprocessing does not begin until after the images have been captured; cameras and lenses have always been excluded from the exemption. Although the conventional process and the digital process are fundamentally different, analogies can be made in order to determine which items are exempt. The taxpayer’s engineer admitted that the video camera and the lens serve purposes analogous to the 35 millimeter camera and lens. The lens simply sizes and focuses the image that is transferred to the video camera, which produces an analog signal that is sent to the NCR computer. Both items are used to collect and send information that is converted by the computer into a digital image. Nothing in the record indicates that the video camera and lens primarily serve a processing function.

The same is true for the base power supply and Zyco controller. These items have only an ancillary role in the production of the digital images. The primary purpose of the power supply is to power to the 35 millimeter camera, the black and white camera, and the motors. It also generates a signal to discharge the flash but does not power the Zyco controller, the Zyco ID module, or the video camera. The Zyco controller simply

synchronizes the video camera and the 35 millimeter camera so that they capture the same image at the same time. Neither the power supply nor the Zyco Controller serves a primary purpose of processing the images.

Finally, in its Exhibit #1 the taxpayer suggests that some of the items listed in the audit report as Zyco Controllers are actually Zyco ID Modules. The taxpayer presented no documents, such as invoices, to support this allegation. Because the taxpayer must present sufficient documentary evidence to support its claim (Sprague at 804), it has failed to meet its burden of proving the Department's assessment concerning the Zyco Controllers is incorrect.

Recommendation:

For the foregoing reasons, it is recommended that the Zyco ID Module, the NCR computer, the NCR monitor, the Pentium computer, and the Sony printer are exempt from tax on the basis that they qualify for the photoprocessing exemption. The taxpayer is entitled to a credit for the use tax paid on these items. It is further recommended that the remaining assessment be upheld.

Linda Olivero
Administrative Law Judge

Enter: